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#78

WORKING PAPER  
OFFICE OF RESEARCH AND ESTIMATES  
CENTRAL INTELLIGENCE AGENCY

WORKING PAPER

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Office of Reports and Estimates  
Northern Branch

BRITISH DIVISION

UNITED KINGDOM

1. Early general election becoming a possibility

A British general election in October or November is becoming a distinct possibility. The decision, which is Prime Minister Attlee's, will probably not be made until after the conclusion of the Washington economic and financial conference in September. But if, as is widely anticipated, the conference fails to produce an agreed and politically acceptable program to arrest the fall in Britain's gold and dollar reserves--and if, therefore, painful adjustments in the domestic economy or continued financial deterioration appear inescapable--the Laborites may seek re-election as soon as a poll can be conveniently held.

Until early summer the evidence pointed to the Labor Party's intention not to call the next general election before spring 1950 (constitutionally, the election must be held by August 1950). By then, it was believed, recovery would have proceeded and the legislative program for Labor's "first five years" would have been accomplished. Britain's rapid financial deterioration, however, became apparent by July and the downward trend in its gold and dollar reserve has continued. Labor Party leaders must by now have reviewed their electoral plans; whether the Party's chances will be better in the fall than in the spring must have been at issue. Failing substantial new US aid as a result of the September conference, the British financial situation is likely to continue to deteriorate. Readjustments in the domestic situation, involving a lower standard of living, will be inevitable. It might seem prudent, therefore, for the Labor leaders to seek their new mandate as early as possible, before the blows have fallen on the populace and before their prestige declines further.

2. US-UK relations under stress

US-UK relations are now being exposed to unusual stress; and if, as seems likely, the forthcoming economic and finan-

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cial conference fails to produce a new program for British recovery involving no substantial cuts in the standard of living, US-UK relations will probably enter a period of acute strain. Only the USSR can benefit from this situation.

Public criticism in the US of the UK government's handling of the British economy developed broadly and rapidly from late July when the UK filed a claim with the OEEC for a greatly increased dollar allocation. It has been fortified by the impression that the UK is taking no new action to cope with its problems, except to appeal to the US for more aid. That much of the criticism of "socialism" and the alleged failure to work hard has little validity worsens the atmosphere in Britain. At all events, the high tide of US criticism is a continuously leading topic in most of the press, where it is often exaggerated; the annoyance has become mutual; and the Foreign Office is unquestionably treating Anglo-US feelings as a matter of major concern. Moreover, the issue is being brought into the field of politics. The Labor Party organ, the Daily Herald, has taken the line that US reactionaries are increasingly anti-Labor, and some Laborite publicists see a systematic attack on socialism by Wall Street and Big Business; the opposition press assails this view on grounds that US criticism is based on the state of the economy and the reserves, not on what reactionaries think about welfare states.

But having a more serious effect on Anglo-US relations will be the coming economic and financial conference. If the outcome is a clear new program promising recovery without serious reduction in the standard of living--a program which must involve new US aid in some form--US-UK relations will at once improve. If, however, as seems more likely at this juncture, no agreed program is developed at the conference and the British come away with little to show for their pleading, US-UK relations can only deteriorate further. A fall general election would become more likely, and relations with the US would probably be an issue; the Labor Party would benefit especially from those US criticisms of its policies which were ill-founded. In the economic sphere the UK would inevitably move further toward the establishment of a highly protective, ultra-discriminatory trade area. This would precipitate new criticism, spreading from US business circles, and US-UK relations would undergo a new strain. (Canada, moving to

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ward economic troubles as a result of British policy, would also enter a period of strained relations with the UK).

Only the USSR would benefit from these developments. To split the US-UK entente cordiale has been an aim of Soviet postwar policy. Easy-to-paint propaganda pictures of the west falling apart could in many eyes acquire more validity.

### 3. British business in Shanghai pressing home Government for freer trade policy

The nature of the commercial pressure the UK Government is under to foster trade relations with Communist China is illustrated in the message despatched to London recently by the British Chamber of Commerce in Shanghai. While repeating the familiar argument about the advantages of keeping a door open to Western influence in China, the message stresses mainly the cost of the contrary policy of acquiescing in the Nationalist blockade of Chinese ports (which it considers doomed to failure in the long run) and proceeding with the wholesale liquidation of British commercial interests in China. Severance pay, forced sales and the like will, it is agreed, make such liquidation impossible without "terrific losses" for British firms. Pointing out that merely "standing by" is already driving some British firms to bankruptcy, the message in effect demands a speedy decision on British trade policy for China--that the Government either break the Nationalist blockade and restore normal consular and communications facilities with Communist China, or tell British firms definitely to cut their losses and pull out.

This type of pressure, of course, represents only one of the factors that the UK Government must take into account in determining its China policy. British business there is both quantitatively greater and qualitatively different from US business--"business in China rather than with China," as one British businessman put it, and to a large extent performing services rather than selling commodities. Since the value of these British interests in Shanghai is so largely their "going concern" value, they are especially likely to suffer from any "wait and see" policy such as serves British interests in Hong Kong for the time being. The UK Government is naturally aware of

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the larger issues involved and certainly will not permit its China policy to be formed on purely commercial considerations; but in its current economic situation the UK is bound to be more sensitive than the US to these considerations, and likely to want full assurance of the absolute necessity of any China policy that will sacrifice British interests there.

#### 4. Syrian coup will probably not affect UK Middle East policy

The Syrian coup of 14 August, though regarded in some Arab circles as so much in Britain's interest as to occasion rumors of British instigation, is unlikely to have any direct repercussions on UK Middle East policy. Syria has never been a major area of British influence. London's main concern over the coup has centered on its possible effects on the general Middle East political situation, and British representatives in Arab capitals were immediately instructed to urge a policy of restraint on the governments to which they were accredited.

Indirect advantage to U.K. interests is suggested by a reference in one of the first communiquees of Col. Hannevi, the leader of the coup, to the "unsuitable foreign policy" of his predecessor; for under the Zaim regime there was abnormal friction between Syria and Iraq and Jordan, traditional spheres of British influence. The statement could also have referred to the terms of the Syrian-Israeli truce agreement, to the granting of permission for the laying of the trans-Arabian pipeline through Syrian territory, or to the reported renaissance of French influence in Syrian affairs.

#### COMMONWEALTH and EMPIRE

#### 5. Britain's financial favors to India and Pakistan

The UK's liberal allocations of sterling and foreign exchange to India a fortnight ago, and to Pakistan within the last few days, have provoked wide criticism because of Britain's financial crisis. They are probably to be explained as a measure of the British Government's concern over India's deteriorating economy and of the importance attached to India's ability to assume the leadership of anti-Communist Asia and thereby preserve the West's eco-

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economic stake in the area. The lenient terms accorded Pakistan follow mainly from the UK's continuing policy of showing no favoritism between the two countries, particularly at a time when there are indications of a rise in anti-British feeling in Pakistan. Another consideration (emphasized by the Government's critics) making for leniency toward both dominions is the need to support the UK export industries supplying these markets and to avoid serious dislocations of trade relations.

In the year ending 30 June, India spent the entire sterling allocation which was to have lasted three years. This expenditure was largely for UK exports for which Britain received no imports in return--and overspent its dollar allocation by about one-third. These overdrafts are being ignored in the new financial arrangements. Moreover, the annual allocation from the blocked sterling balances for the current and succeeding years has been raised from the originally agreed £40 to £50 million annually with a provision for another £50 million if needed this year. With regard to dollars, India is not to receive a specific allocation since it has returned to full membership in the sterling area and has agreed, like other Commonwealth countries, to endeavor to cut its total dollar spending by 25%. Full sterling area membership, however, will enable India to draw whatever dollars it needs from the central reserves, and it appears that it is actually counting on the availability of more dollars than last year. This generous agreement will impose a heavy strain on the UK, considering its present economic straits. Having been liberal with India, it followed that Pakistan would receive comparable treatment, and the same is likely to hold true for Ceylon. Releases from the blocked sterling balances of these countries largely end up as payments for UK exports, the so-called "unrequited" exports in return for which Britain receives no imports.

#### Union of South Africa

##### G. Cabinet discusses economic crisis and India-Pakistan request for conference

The first cabinet session since Parliament's adjournment on 30 June was called by Prime Minister Malan on 16 August chiefly for consideration of the Union's criti-

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cal economic situation. Though Minister of Economic Development Eric Louw announced recently that there could be no further exchange allocations this year because the £55,000,000 allocated to imports for the remainder of 1949 had already been exhausted, Cabinet decisions will probably remain tentative. Comprehensive remedial measures will hinge upon the results of Finance Minister Havenga's loan negotiations in London and Washington. (On 18 August Havenga arrived in the US for a month to raise a dollar loan and to try to induce the International Monetary Fund to increase the world gold price at its September meeting.)

Another matter up for cabinet discussion is the India-Pakistan request for a round-table conference on the Union's treatment of its Indian minority. South Africa has already indicated that the agenda for such talks must include the repatriation of its Indian community to India and the cancellation of India's trade boycott against the Union.

#### 7. Cabinet shifts

Just prior to the cabinet meeting the Prime Minister announced a reappointment of four relatively minor portfolios ostensibly to distribute work more equitably among the twelve Ministers and to relieve pressure on Eric Louw in particular. The portfolios were reassigned, however, to the cabinet's increasingly influential "wild men", thus further strengthening the ultra-reactionary wing of the Nationalist Party. This action indicates that Malan is not apprehensive of Havenga's declining to merge his moderate Afrikaner Party with the Nationalists in November.\*

#### 8. Malta raises a problem for the UK

Malta's demand that it be permitted to seek direct ECA aid from the US will be rejected by the UK Government, but the British will probably have to resume subsidization of the Maltese economy. War-shattered, overpopulated (300,000 people in 122 square miles), strategically-important Malta has so far been able to stave off inflation and unemployment by large British grants for reconstruction and contributions to Maltese food subsidies and by abnormally high employment in the Admiralty dockyards, the largest

\*See IB Weekly #37, 6 June 1949

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employer on the island. Reconstruction is still going on though the fund will run out in 1954. British contributions to the food subsidies stopped in March. The Admiralty has decided to fire 1200 of the 12,000 dockyard workers. The Maltese, who feel that Britain has interpreted less than generously Churchill's pledge that Malta would be paid back "every penny" of what the war had cost her, also believe that they have not received their fair share of the UK's ECA funds. The Maltese enjoy virtually full self-government except for foreign affairs and defense, and since last September they have been seeking permission to participate in OEEC on their own and to apply for direct ECA aid. On 8 August the Maltese Government delivered an ultimatum to the British Colonial Office that "grave steps" would have to be taken unless an adequate reply were received by 22 August to Malta's claim to direct participation in OEEC.

What "grave steps" were contemplated is not known, but it is doubtful if, as a Soviet broadcast claimed, the Maltese planned to "withdraw from the British Commonwealth" and "raise the flag of the United States." Malta's Prime Minister Boffa now seems to be wavering in his determination to stand by the ultimatum. On 15 August, his Deputy Prime Minister resigned because Boffa would not assure him that the ultimatum would not be withdrawn. Boffa, who claimed support from the rest of his Cabinet, refused to accept any limitations on his powers of negotiation. It is likely that the continuing conference between Boffa and Colonial Secretary Creech-Jones will culminate, not in Malta's being permitted to request direct ECA aid, nor in any "grave steps" being taken by the Maltese Government, but rather in renewed British financial help to keep Malta's economy ticking.

## IRELAND

### 9. Irish to continue to press for solution of Partition dispute

Irish spokesmen will continue their efforts to raise the Partition question in the arenas of international politics, despite their failure at the Council of Europe. They are required by the tenets of their nationalism and the realities of their political futures. To make Par-

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tion an international dispute that international organizations cannot ignore has become a principal aim of Ireland's foreign policy.

NORTH AMERICAN DIVISION

CANADA

1. The Canadian background for the Washington talks

The Canadian position on the British financial crisis is still as it was in the London talks,\* and it is expected that Canada will not present a specific program for solution of the UK's problems. There are several reasons for this. Canadian official opinion is that the UK's problem is primarily one of internal adjustment. Further, there is a feeling in Canada that it has done everything possible to aid the UK both by loans and by the encouragement of imports from Britain. In addition, there has been a marked deterioration in Canada's own foreign trade position this year which merits priority attention. Import controls on dollar purchases are expected to be increased while first priority is being given to efforts to increase exports to the US-- Canada must halt the drain on its supply of US dollars as Europe's hard currency purchases in Canada decline.

The Canadian attitude does not mean that the Dominion will do nothing, but merely that the first move is up to the UK. Canada's interest in solution of the problems is great. Should Britain retreat further into sterling bloc trading or should a devaluation of the pound become necessary, the effects on the Canadian economy would be far-reaching. It is expected that if the UK is willing to make changes in domestic policies Canada will do all it can to assist.

\* See NB Weekly #73, 13 July 1949

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SCANDINAVIAN DIVISION

ICELAND

1. National elections in October

New elections, scheduled for a three-day period beginning 23 October as a result of the President's pro-roguing of the Althing (Parliament on 12 August,\* should produce a more effective Icelandic government than that based on the three-party coalition formed in February 1947. An election campaign waged over current issues and a new mandate from the electorate are required to clarify the political situation in Iceland. Communist prospects for participation in the new government are nil.

\* See NB Weekly #77, 15 August 1949

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